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INTEGRATING TRADE, ENVIRONMENT AND DEVELOPMENT: RECENT PROGRESS AND OUTSTANDING ISSUES

Report by the UNCTAD secretariat

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I. INTRODUCTION

1. In recent years, intergovernmental deliberations in UNCTAD, WTO, the Commission on Sustainable Development (CSD) and the OECD have contributed to a better understanding of trade and environment linkages. The CSD has played an important role in promoting cooperation and complementarity in the work of WTO, UNCTAD and UNEP and in identifying gaps, as well as in bringing the civil society to international deliberations. In parallel with intergovernmental deliberations, there has been more dialogue and coordination between trade and environment ministries at the national level, as well as increased involvement of non-governmental organizations (NGOs) and the business community in the trade and environment debate.

2. The debate has shown that it is difficult to draw generalized conclusions on how compatibility between trade and environmental policies can best be achieved. Generally it is not trade that is at the root of environmental degradation, but rather unsustainable production and consumption processes.[1] This has important implications for choosing and implementing effective policy measures. To the extent that the multilateral trading system (MTS) does not impose significant restraints on the implementation of effective environmental policies and measures at the national and international levels,[2] more emphasis has to be given to an identification of an agenda that promotes mutual supportiveness between trade, environment and development. It follows that the international debate has to go beyond the consideration of narrowly defined conflicts between trade rules and environment protection to a holistic consideration of all factors relevant to the formulation of sustainable development policies.

3. From a development perspective, several viewpoints on the trade and environment interface have been expressed. First, it is contended that poverty is a basic cause of environmental degradation in many developing countries, and that the contribution trade can make to the eradication of poverty by raising income levels is an indispensable requirement for the promotion of sustainable development. Second, where trade-related environmental measures may create high adjustment costs for developing countries' exporters, there is a need to ensure flexibility and fairness in the implementation of environmental policies. Third, policy measures applied to promote the internalization of environmental costs should seek to avoid distortion in international trade and investment, and measures to improve environmental conditions in one country should not shift the costs to others.

4. Furthermore, for many developing countries, in particular the least developed among them, increasing the ability to respond effectively to environmental challenges requires that high priority is given to developing their economic capacities. Thus, the environmental problems and priorities of low-income, commodity-dependent countries and other countries which remain marginal participants in world trade are often different from those of other countries. Expansion and diversification of their export opportunities, including diversification into higher value-added products, could help these countries in their efforts to both reduce poverty and protect the environment.

5. These considerations are reflected to some extent by the shift in emphasis in the debate on trade and environment. Issues which earlier were viewed by some

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[1] Similarly, trade liberalization has mainly indirect effects on the environment, through induced changes in production and consumption patterns. Negative environmental effects, if any, could be addressed by appropriate supporting environmental policies at the national level.

[2] The Report of the WTO Committee on Trade and Environment (CTE) states that "Discussions have demonstrated that the multilateral trading system has the capacity to further integrate environmental considerations and enhance its contribution to the promotion of sustainable development without undermining its open, equitable and non-discriminatory character". WTO, Report (1996) of the Committee on Trade and Environment, para. 167. PRESS/TE 014, 18 November 1996.

as a potential source of conflict, would now appear to have been set aside. Examples can be found in particular in the competitiveness debate (e.g. on issues such as "eco-dumping"). However, new issues of concern have emerged. For example, the debate has evolved from the early position in which developing countries were primarily concerned about the use of environmental policies and measures for protectionist purposes or to create new forms of conditionality to the current position in which many developing countries have taken a pro-active stance, adding to the international agenda a number of issues of particular interest to them, such as market access, access to and transfer of environmentally sound technologies, and the issue of exports of domestically prohibited goods.[3]

6. Achieving additional progress on the trade and environment debate, apart from building further understanding and confidence between different communities, requires appropriate consideration of the concerns and interests of all countries. In addition, in building compatibility between trade and environment, there is a need to further examine the flexibility of trade principles to accommodate current and emerging environmental policies and vice versa. The Commission's review of progress in integrating trade, environment and development and outstanding issues, in particular by furthering understanding of the development dimension, can help in ensuring a balanced and integrated approach in the future trade and environment debate.

7. The Commission's deliberations are also important in the context of the preparations for the first five-year review of progress achieved in the implementation of Agenda 21 (adopted by the United Nations Conference on Environment and Development (UNCED), Rio de Janeiro, June 1992), to be undertaken by the Commission on Sustainable Development (the fifth session of the CSD will be held in New York from 7 to 25 April 1997) and the Special Session of the General Assembly (23 to 27 June 1997).[4] Consequently, the analysis on "recent progress" generally takes UNCED and its results, as embodied in the Rio Declaration and Agenda 21, as a point of reference.

8. This report is presented in four sections. Section II outlines the debate on some specific issues, highlighting progress made as well as some unresolved issues. Section III examines some outstanding issues which cut across the items discussed in section II, some of which may be addressed in future UNCTAD activities. The conclusions and recommendations are contained in section IV. A note describing UNCTAD's activities on trade, environment and development will be issued as report TD/B/COM.1/Misc. 2 (English only).

II. RECENT PROGRESS ON KEY ISSUES

9. This section reviews progress since UNCED on key issues of the trade, environment and development debate, focusing on the different items listed in para. 91 (iv) of the final document of UNCTAD IX, i.e. competitiveness, market access, eco-labelling, multilateral environmental agreements, positive measures and the relationship between trade liberalization and sustainable development. It is, however, recognized that some of these items are interlinked.

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[3] Moreover, it is recognized that trade and environment need not divide countries on North-South lines. For example, natural-resource-rich countries in the North and the South have similar interests in considering trade liberalization in natural-resource based products, in the context of sustainable development. Similar North-South alliances exist with regard to further trade liberalization in agriculture.

[4] The General Assembly requested UNCTAD to report, through the Commission on Sustainable Development, to the Economic and Social Council and the General Assembly, at its special session in 1997 on the concrete progress achieved on the issue of trade and environment. (Resolution 50/95 of 12 December 1995, paragraph 26.) The corresponding report has been included in the list of main documents for consideration during the 1997 Review by the Commission on Sustainable Development.

A. Competitiveness

10. It is important to make a distinction between competitiveness at the firm or sector levels and the concept of national welfare. Loss of competitiveness by some sectors can be compensated by gains elsewhere. National welfare is not simply a linear aggregation of the competitiveness of individual firms. Analysing it requires a much broader consideration of a wider set of issues which could include factors such as productivity, technological innovation, investments, export and import prices, trade and capital balances, working conditions, taxes, political stability, environmental and health improvements etc. In addition, in calculating national welfare, micro-economic (environmental) costs have to be discounted by cost-saving environmental benefits (e.g health expenditure or forest rehabilitation costs).

11. A significant development since UNCED is that Governments have taken a strong view against demands for "levelling the competitive playing field" for differing environmental policies across countries; in UNCTAD and the Commission on Sustainable Development, developing countries have joined OECD Governments in firmly rejecting demands sometimes made to introduce so-called "green countervailing duties", or other protectionist or WTO-inconsistent trade measures, to compensate for negative competitiveness effects, whether real or perceived, of environmental policies".[5] Thus, as long as environmental policies comply with the principles of the multilateral trading system, their effects on competitiveness has been set aside as a relevant issue for trade rules. It is, however, important to examine the competitiveness effects of environmental policies from the perspective of environmental and developmental policy-making.

12. Systematic - positive or negative - links between environmental protection and international competitiveness have not been identified. According to one hypothesis, increased environmental protection raises production costs for firms and thus adversely affects competitiveness. Another hypothesis suggests that strict environmental regulations can actually lead to cost savings and improved competitiveness by inducing firms to increase efficiency, improve resource management, and avoid waste; by stimulating cost-offsetting or value-adding innovations, by producing marketing advantages in the growing market for environmentally friendly goods, and by enhancing a country's potential to supply environmental goods and services internationally.[6] Others maintain that environmental protection costs are small and that they do not constitute a major policy issue.

13. Empirical and analytical work done at UNCTAD suggests that each of these three perceptions is too narrow. Indeed, many factors have a bearing on the competitiveness effects of environmental policies, including firm or sector-specific factors, general factors which may vary with the level of development, such as the availability of environmental infrastructure, and government policies. In addition, competitiveness effects may depend on who decides what and when to internalize and whether the decision is taken on the basis of cost-benefit analysis. It follows that similar measures may have differential effects on developed and developing countries. There is concern that environmental measures and requirements may adversely affect the competitiveness and market access opportunities of small and medium-sized enterprises (SMEs) especially in developing countries (See Box 1). Future work on competitiveness (and market access) could therefore focus on specific sectors and on the case of SMEs, an issue which is further elaborated in section III.

14. Competitiveness effects of environmental policies, however, can be addressed by appropriate policies at the national and international levels.

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[5] UNCTAD, Final Report of the Ad Hoc Working Group on Trade, Environment and Development, and Commission on Sustainable Development, fourth session, Decision on Trade, Environment and Sustainable Development.

[6] These opportunities may not be easy to access by some producers, particularly small and medium scale enterprises (SMEs) in developing and least developed countries.

Box 1

Difficulties that SMEs may encounter in responding to environmental challenges

Fixed costs of installing environmentally sound technologies (ESTs) may be high for small firms. It may be difficult to sustain the period of adaptation. There may be a long period between installation and the time investments are recovered.

Variable costs may be relatively high for SMEs. In addition, environment-friendly input materials, which may represent a considerable portion of total variable costs, may be expensive.

SMEs may find difficulties in passing on increased costs to the consumer, because of the highly competitive nature of the markets in which they operate. Large firms may be in a better position to pass on at least a part of the increased costs to the consumer, e.g. because their brand names are well established. Consequently, SMEs tend to be reluctant to take on any cost increases.

Lack of finance is a problem, since SMEs often cannot themselves finance investment and credit may not be available for environmental investments. Therefore, financial constraints inhibit modernisation of production processes. Large units, because of their organizational strength and established position in the financial markets can obtain funds at a lower cost. Banks often prefer to lend to larger firms, because of the risk factors.

Access to technology is also a problem since SMEs may find it difficult to identify and adapt environmentally sound technologies (ESTs). In particular this may be the case because ESTs may require certain economies of scale. For example, chemical recovery systems are not adapted for small paper mills.

Difficulties in obtaining environment-friendly input materials may be experienced by SMEs (e.g. dyes or chemicals). Once a new requirement emerges from an external market, a long time often passes before substitutes become available on the domestic market. While large firms may engage themselves in import activities or can influence their domestic suppliers to switch to environment-friendly materials, such opportunities may not be readily available for SMEs.

Difficult access to information is another problem. While large firm get timely and accurate information from importers in developed country markets and various other sources, SMEs rely heavily on Government sources, often implying considerable time delays.

Source: UNCTAD and Manas Bhattacharyya, "Small is not always beautiful", Economic Times, India, 5 November 1996.

Capacity-building, the provision of information, support to access technology and innovation, infrastructure, testing and certification, etc. are of key importance. Furthermore, consultations between industry, government, NGOs and other stakeholders when preparing environmental policies could help to set realistic requirements and ensure industry cooperation.

15. Thus, the debate is increasingly moving from the stage of problem identification to the discussion of possible solutions. This development is particularly important to the extent that environmental policies (e.g. increased efforts to avert the problem of climate change) may have stronger trade and competitiveness effects in the future (see box 2).

B. Market access

16. Market access issues fall within, but are not limited to, the realm of trade rules. Market access concerns may arise on account of external environmental requirements.

17. In addressing the question whether existing trade rules provide sufficient safeguards (including through their transparency provisions), to deal with environmental policies which have significant trade effects, discussions have focused on two sets of issues: (a) are environmental requirements different from other measures covered by provisions in the WTO? and (b) how have environmental policies affected market access, particularly for exports from developing countries?

18. The first set of issues has been debated inconclusively in various fora. Some argue that environmental standards are no different from other regulations covered by the Technical Barriers to Trade Agreement (TBT). Others argue that environmental standards are different from other regulations and requirements in that they comprise measures: (a) which are largely voluntary (for which the existing body of trade rules is less developed); (b) which are often based on PPMs (according to most interpretations standards based on non-product related PPMs are not covered by trade rules);[7] (c) for which channels of notification are less well established (there is some ambiguity about their coverage by WTO transparency obligations); and (d) based on the precautionary principle (the provisions of the TBT Agreement are ambiguous on this issue).

19. On the second set of issues, while environmental policies in developed countries do not have generalized effects on market access for developing countries, UNCTAD's country case studies indicate that environmental measures and requirements may affect competitiveness and market access opportunities for firms in some sectors and, in particular, SMEs. In this context, the CTE has recognized that "Further work is needed to ensure that the implementation of environmental measures does not result in disguised restrictions on trade, particularly those that have adverse effects on existing market access opportunities of developing countries".[8]

C. Trade liberalization and the environment

20. Environmental benefits are expected to accrue from trade liberalization to the extent that it results in (a) a more efficient allocation of resources, including environmental resources; and (b) economic growth and development, thus generating additional incomes which can be channelled to environmental improvements and increasing demand for environmental protection. In the context of developing countries, trade liberalization and the consequent export expansion and growth, are likely to bring additional environmental benefits through reducing poverty and the associated environmental damages.

21. Measures cited in this context are tariff escalation and tariff peaks, production and export subsidies, high internal taxes particularly on tropical products, export restrictions and export taxes, the export practices of state trading enterprises, and various non-tariff barriers.

22. Environmental benefits are expected to accrue in a variety of ways. Some consider they accrue most directly through the removal of trade restrictions on environmentally-friendly goods and environmental services; they will accrue also through the removal of restrictions on the transfer of environmentally-sound technologies; in addition, trade restrictions and distortions can lead to an

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[7] To the extent that consumer concerns about environmental effects associated with upstream stages of a product's life cycle have a significant influence on the market place, PPMs could be considered as a determinant of "product quality".

[8] WTO, op. cit., para. 199.

Box 2

Climate change : policies and measures for "common action"

Much of the future debate on the relationship between environmental policy, competitiveness and market access will be related to the problem of climate change.

In the context of the work of the Ad Hoc Group on the Berlin Mandate, an expert group is making an initial assessment of a range of cost-effective policies and measures which lend themselves for "common action" by Annex I countries (developed countries and some countries in transition). Even though these policies and measures would be taken by Annex I countries only, they may have -positive or negative- economic effects on developing countries. Thus, while developing countries expect developed countries to take the lead in combating climate change, at the same time there is a certain level of concern about the effects of policies and measures on their exports to developed country markets.

It may be useful, for analytical purposes, to distinguish two groups of policies and measures. The first group consists of economy-wide policies and measures, such as energy taxes and subsidy elimination; effects on non-participating countries vary widely from case to case. Models have been developed to assess these effects on different groups of countries. An examination of the results of these models, however, falls outside the scope of this report.

Another group consists of sector- and product-specific measures, such as energy efficiency standards. Here, the analysis contained in section II of this report is relevant. Some experience has been acquired with measures applied by individual countries. However, in the case of policies and measures taken through "common action" both the potential effects on competitiveness as well as the opportunities for facilitating measures aimed at alleviating any negative and strengthening any positive effects may be larger.

While "common action" at times may reduce trade and competitiveness effects on non-participating countries (e.g. harmonisation of product standards as well as of testing and certification procedures may reduce transaction costs), in most cases "common action" may increase the potential economic costs to developing countries simply because more countries apply a given policy or measure and because "common action" stimulates measures that would not be feasible if applied by individual countries.

By the same spoken, it appears important to examine how "common action" can facilitate "positive" measures to support sustainable development policies in developing countries. Initiatives in the area of facilitating information on, access to and transfer of environmentally sound technologies, voluntary measures in the area of foreign direct investment, additional market access for climate-friendly products, etc. are of key importance and should be further examined.

With appropriate measures in place, international trade and investment links may result in policies and measures taken by Annex I countries having trickle down effects on non-parties and stimulate the diffusion of more efficient technologies to these countries. It is important to identify win-win situations, where developing countries can simultaneously raise export competitiveness as well as lower energy consumption costs and reduce emissions.

inefficient allocation of resources, hold back income growth, particularly in developing countries, and artificially shift resources into activities which

place additional pressure on domestic, environmentally sensitive resources; reducing or removing them would help to correct this. Some others also consider that to ensure direct and substantial environmental benefits, trade liberalization should be complemented by measures to improve market access, access to environmentally-sound technologies, finance and capacity building.

23. Agenda 21 stressed the important role of trade liberalization in achieving sustainable development. Since UNCED, progress has been achieved, in particular through the completion of the Uruguay Round negotiations. The timely implementation of the corresponding commitments is of key importance. The challenge is now to further build on the synergies between trade liberalization, economic reform and enhanced environmental management. In many developing countries, trade liberalization and expansion have already made important contributions to poverty alleviation and reducing associated environmental stress. Additional initiatives may be needed, in particular in favour of those countries which have not participated in the recent growth of world trade. In this context, the Midrand Declaration (in the section on globalization) recalls that "The least developed countries (LDCs), particularly those in Africa, and other developing countries remain constrained by weak supply capabilities and are unable to benefit from trade. Marginalization, both among and within countries, has been exacerbated".

24. A large part of the discussion on trade liberalization and the environment has focused on the adverse environmental effects of the subsidization of agricultural production and exports. These are described as arising, among other factors, from intensified land use, increased application of agro-chemicals, loss of natural wildlife habitats and biodiversity, and the expansion of agricultural production into marginal and ecologically sensitive areas. Agricultural assistance through output-related policies in many OECD countries was shown to have imposed high environmental costs in those countries at high financial expense. It also imposed high economic and environmental costs on other countries with a comparative advantage in agricultural production and trade, particularly developing countries.[9]

25. A counter argument notes that the effect of trade liberalization on prices cannot be predicted with certainty, and that adjustment of prices is not a priori environmentally efficient. Such environmental efficiency would depend to a certain extent both on wider economic factors in agricultural markets and the conditions conducive to structural adjustment in producer economies. Furthermore, market mechanisms could only lead to both an economically and ecologically optimal allocation of production resources if full internalization of environmental costs were achieved. Moreover, it is contended that environmental benefits from trade liberalization would accrue from domestic reform in agricultural policies. This analysis could be extended to other sectors.[10]

26. Where trade liberalization does not bring environmental benefits, it should be accompanied by complementary environmental and resource management policies, if its full potential contribution to better protecting the environment and promoting sustainable development through more efficient allocation and use of resources is to be realized.

D. Eco-labelling

27. The debate on eco-labelling indicates the challenge that arises on account of the fact that, whereas eco-labelling, being based on the life cycle approach (LCA), may lead to the development of criteria on non-product related PPMs, the international trading system is based on the "like product" approach. This potential conflict may be heightened to the extent that specific PPM-based criteria may not be as environmentally beneficial to the exporting country as they are to the importing country.

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[9] See also: WTO, op. cit. para. 112.

[10] See also: WTO, op. cit. para. 118.

Box 3

Number of product categories and of products under different eco-labelling programmes

September 1996

	Product categories for which criteria are established	Eco-labels granted			
		Prod. categ.	Manu-facturers	of which foreign	Pro-ducts
Canada	96	36	127	13	>1,600
Nordic countries	43	28	n.a.	n.a.	>1,000
European Union	12	4	11	none	24
Japan	71	68	1,050	29*	2,021
Germany	74	63	754	107**	3,206
Taiwan Prov. of China	34	19	85	3	370
Singapore	21	18	140	13	542
Rep. of Korea	35	32	122	none	169
France	5	2	34	4***	231

* Including Japanese trading companies, foreign subsidiary companies of Japanese companies, joint venture companies, and foreign manufacturers who have concluded contracts for the use of the label in the name of their Japanese importers.

** Foreign manufacturers who have concluded contracts for the use of the label in the name of their German importers are not included.

*** From other EU countries

28. Eco-labelling can have different types of trade effects. Their significance depends to a large extent on the importance of eco-labelling in the market place. In many cases, trade impacts may be relatively small because eco-labelling targets only certain segments of the market, or because markets fail to react to eco-labelling. Effects may become more important, however, to the extent that market responses become more significant.[11] Box 3 shows the number of product categories and labelled products under different eco-labelling programmes.

29. Progress has been made in building consensus on certain principles to guide the operation of eco-labelling progress, in particular, with regard to the process of developing environmental criteria, procedures on conformity assessment, transparency, and equal access for domestic and foreign companies to the eco-label. The International Organization for Standardization (ISO) has been developing international standards, as part of the 14000 series of standards on environmental management, to which eco-labelling bodies can adhere on a voluntary basis. These standards provide useful guiding principles for the operation of eco-labelling programmes, covering, inter alia, product environmental criteria, transparency, trade aspects, accessibility and mutual recognition.

30. Similarly, "the CTE felt that an important starting point for WTO Members to address some of the trade concerns raised over eco-labelling

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[11] As a follow-up to its work on PPMs and life-cycle management, the OECD is undertaking a case study of the actual market, trade and environmental effects of eco-labelling programmes operating in OECD countries.

schemes/programmes is by discussing how to ensure adequate transparency in their preparation, adoption and application, including affording opportunities for participation in their preparation by interested parties from other countries. The transparency provisions contained in the TBT Agreement, including the Code of Good Practice for standardizing bodies contained in Annex 3 of the Agreement provide a reference point to the further work of the CTE in enhancing transparency of eco-labelling schemes/programmes".[12]

31. Little progress has been made, however, in dealing with the issue of non-product related PPMs. The relevant ISO standards, while recognizing and, to some extent, encouraging the use of LCA, do not address this issue in any detail. The only guiding principle which can help to address the trade aspects of non-product related PPMs is that of mutual recognition.

32. Mutual recognition, however, is a complex issue. Mutual recognition is easier to achieve when the environmental conditions and priorities in the two countries are comparable, and some initiatives have already been taken. For example, the "Green Seal" programme in the United States and Canada's "Environmental Choice" programme have entered into an informal understanding enabling mutual recognition, provided that the two programmes develop similar criteria for the product in question. There is also a formal agreement between the eco-labelling programmes of Canada and Taiwan Province of China. An interesting concept here is that in case that the two programmes use different criteria, the use and disposal criteria of the programme in the importing country and the RPM-related criteria of the programme of the exporting country should be met. However, consumer acceptability and programme credibility must be considered, and mutual recognition may not be granted if the criteria are substantially different.[13]

33. Furthermore, the usefulness of the concept of mutual recognition is reduced to the extent that it requires that an eco-labelling programme exist in the exporting country, something that has been difficult in developing countries. The concept of equivalency provides more flexibility in that it does imply such requirement. Although several fora have recommended the exploration of the concept of equivalency, little progress has been made. For example, attempts to reflect this concept in the ISO guidelines have not been successful.

E. Multilateral environmental agreements

34. While the large number of multilateral environmental agreements (MEAs) clearly show the willingness and ability of the international community to deal with global environmental problems on the basis of multilateral cooperative approaches, some discussion has focused on the instruments and measures used to implement MEAs. Discussions in this area have focused on two key issues. First, to what extent are the relevant principles contained in the Rio Declaration and Agenda 21, in particular those related to sustainable development, incorporated into existing and new MEAs? Second, the relationship between trade measures used within the framework of MEAs and the rules of the multilateral trading system, an issue which is under examination in the CTE.

35. In the debate on both these issues, a number of questions have emerged, including: what range of policy instruments is available to achieve the objectives of an MEA and how can the effectiveness of different policy instruments be assessed, in particular have trade restrictions been effective in meeting environmental goals? What are the economic and developmental effects of MEAs, and the different instruments used therein, on developing countries? How can the participation of developing countries in an MEA, as well as their economic capacity to meet its environmental objectives, be promoted, in harmony

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[12] WTO, op. cit., para. 184.

[13] N. Yu, J. Hung, J. Polak and E. Bozowsky, "Feasibility study on mutual recognition between the Green Mark and Environmental Choice Eco-labelling Programs", paper presented at the 1996 Annual Meeting of the Global Eco-labelling Network.

with the principle of common but differentiated responsibilities?

36. Comparative analysis of different MEAs has shown that there are considerable differences between trade and other provisions of different MEAs, in particular the kinds of trade measures that the parties are authorized or required to apply and the conditions pursuant to which the measures are taken. Nevertheless, discriminatory trade restrictions applied in the context of an MEA can involve extra-jurisdictional action which would be inconsistent with WTO rules. This possible contradiction has raised doubts and some have argued that there is a need for clarification of the relationship between WTO provisions and these trade measures. This issue is being discussed in the CTE.

37. Discussions have also focused on the necessity of trade measures in achieving the environmental objective of the MEA, including through a consideration of: (i) the effectiveness of the trade measure in achieving the environmental objective; (ii) whether the measure is the least trade-restrictive or distorting; (iii) the cost-effectiveness and developmental effects; and (iv) the proportionality of the measure to the need for trade restriction to achieve the environmental objective. Considerations on equity have also been raised in this context. According to some observers discriminatory trade restrictions against non-parties to an MEA may be an unequitable way to pursue international environmental objectives.

38. Many have argued that a renewed commitment needs to be taken by the international community to avoid using trade measures unilaterally for environmental purposes. In discussions on such a renewed commitment, differing views have been expressed as to what constituted "unilateralism". This is particularly important in view of the fact that there is no agreed definition of what constitutes an MEA.[14]

39. Another view that is rapidly gaining ground is that, because MEAs use a package of measures, it is difficult to evaluate which of these measures are more effective in achieving the targets. The range of policy options for achieving environmental objectives of MEAs include permits, quotas, market based instruments, trade measures and positive measures, such as access to technology and finance. As the package may contain a balance between trade measures and positive measures, mechanisms are required to ensure that the latter are fully implemented. These issues have repeatedly come up in discussions of the conference of parties under the Montreal Protocol. A related issue is the design of innovative positive measures which could include the involvement of the private sector in MEAs.

40. From a development perspective, it is important to note that, while yielding global environmental benefits, MEAs may have broad economic effects. The costs of environmental standard implementation, which are borne at the national level, can differ widely among parties to an MEA, based on variables such as the dependency of the economy on the product subject to control, specificity of the standard, the availability and adequacy of substitutes, the degree of patent protection of specified technologies, administrative costs and other factors. Costs may also vary in accordance with the levels of economic development and existing environmental standards prior to the introduction of the international standard[15].

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[14] Some suggest that a genuine "multilateral" consensus requires that: (i) negotiation of and participation in an MEA to be open on equitable terms to all interested countries; (ii) broad participation of interested countries in both geographical terms and representing varying levels of development; and (iii) adequate representation of consumer and producer nations of the products covered by the MEA.

[15] UNCTAD, 1996, Environment, Competitiveness and Trade: A Development Perspective. A paper prepared for the Topical Seminar in Preparation of UNCTAD IX, Helsinki 18 and 19 January, 1996.

41. A recent Global Environmental Facility/World Bank study notes that, although an action may be justified economically from the viewpoint of the entire global community, it may impose an "added burden" financially on a given country; "by allocating at least this incremental cost to the international community as a whole, the country undertaking the action will be left no worse off financially. Cost sharing is particularly important to developing countries because they are unable to bear the financial burden implicit in protecting the environment"[34].

42. This concept has been built into some MEAs. For example, technically, the Multilateral Fund of the Montreal Protocol Fund should meet the full incremental costs of phaseout by developing countries. In practice, however, these costs are hard to define and beneficiary developing countries have had to bear at least some of the cost. In addition, a distinction should be made between "voluntary" and "imposed" costs. Voluntary costs are voluntarily accepted by a country in order to mitigate the global environmental problem. In the case of the Montreal Protocol, for example, voluntary costs are costs incurred by a party through phasing out ODSs (e.g. cost of capital conversion, royalties, etc.). Imposed costs, however, are costs that are imposed anyway by adaptation to or damage resulting from ozone depletion, by international trade restrictions on non signatory or noncomplying countries, or by increases in the economic cost of producing ODS and ODS technologies for a shrinking international market.[35] An interesting question is whether the use of trade measures increases the imposed costs of an MEA and whether imposed costs should in some way be taken into account in the design and implementation of positive measures.

43. More empirical studies on the economic effects of MEAs are needed. The CSD, at its third and fourth sessions, invited UNCTAD and UNEP, to analyze the effects of trade measures and other policy instruments in MEAs on the achievement of environmental goals and on trade and competitiveness of developing countries and countries with economies in transition and how positive measures can assist those countries in meeting their obligations under the agreements. The UNCTAD secretariat is cooperating with UNEP in a project aimed at examining the contribution of different policy instruments, including both trade measures and positive measures, to achieving the environmental objectives of MEAs. The project will draw from the experience of selected developing countries with regard to three MEAs, i.e. the Montreal Protocol, the Basel Convention and the Convention on International Trade in Endangered Species (CITES).

F. Positive measures

44. Intergovernmental deliberations have increasingly emphasized the role of positive measures in integrating trade, environment and development. The Ad Hoc Working Group on Trade, Environment and Development[36], the CSD[37], UNCTAD IX[38]

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[34] King, K. and M. Munasinghe, 1995. Ozone Layer Protection: Country Incremental Costs. Global Environmental Facility and the World Bank.

[35] King, K. and M. Munasinghe, op. cit. page 3.

[36] UNCTAD, Final report of the Ad Hoc Working Group on Trade, Environment and Development incorporating the report on its third session, TD/B/42(2)/9 and TD/B/WG.6/11, Paragraph 48.

[37] See, for example, Report of the Commission on Sustainable Development on its third session (Official records of the Economic and Social Council, Supplement 12 (E/1995/32), paragraph 61.

[38] A Partnership for Growth and Development, (final document of UNCTAD IX), para. 71.

and the CTE[21] and the General Assembly[22] have recognized that positive measures can be effective instruments to assist developing countries in achieving the objectives of sustainable development and in meeting the multilaterally-agreed objectives of MEAs. While progress has thus been made in building consensus on the importance of positive measures, further analytical work and action-oriented projects are needed to identify strategies for the design and effective implementation of such measures. Innovative approaches are needed, in particular since in a number of cases the implementation of positive measures may face financial constraints. The CSD, at its fourth session, encouraged UNCTAD "to propose positive measures at the national and international levels, aimed at supporting developing countries in their efforts to achieve the objectives of sustainable development, focusing on capacity building and support for national efforts aimed at internalizing environmental costs".[23]

45. Both the Rio Declaration and Agenda 21 have enumerated a number of positive measures. Such measures, however, have not been defined in a comprehensive manner. Positive measures constitute a cross-cutting and constantly evolving issue, and further proposals should emerge from the analysis and debate of various items on the trade and environment agenda. For analytical purposes, however, positive measures can perhaps be grouped into two main categories: (a) measures aimed at countering undesirable adverse income and developmental effects of environmental policies and measures, inter alia in the context of MEAs; and (b) policies and measures aimed at creating and/or strengthening positive linkages between trade and environment policies. Positive measures also include capacity-building.

46. Concerning the first category of positive measures, Agenda 21 called inter alia for access to and transfer of technology and access to finance. For example, positive measures have been incorporated into MEAs, in accordance with the principle of common but differentiated responsibilities. Although the importance of these measures has repeatedly been reiterated at the intergovernmental level, widespread implementation in the post-UNCED period has faced a number of constraints. Innovative approaches may be needed, including in the context of mechanisms that promote the transfer of environmentally sound technologies (ESTs) through foreign direct investment.

47. The analysis on competitiveness and market access indicates that this category of positive measures also includes investments in environmental infrastructure, dissemination of information, technical assistance, capacity-building, bilateral cooperation and the provision of adequate time to adjust to new environmental requirements.

48. With regard to the second category, creating and/or strengthening positive linkages between trade and environment, the above analysis, for example on competitiveness and trade liberalization, has stressed the need to identify "win-win" situations, including for SMEs. In a much broader context, positive measures aim at harnessing the synergies between trade liberalization, economic reform, improved management of natural resources and the environment, involving the business community and the civil society in the design of specific enabling

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[21] In its report, the CTE noted that "Positive measures, such as access to and transfer of technology both according to the terms and conditions stipulated in the covered MEAs and without prejudice to the requirements of the TRIPs Agreement can be effective instruments to assist developing countries to meet multilaterally-agreed targets in some MEAs and in keeping with the principle of common but differentiated responsibilities in the Rio Declaration". WTO, op. cit. para. 207.

[22] General Assembly, Resolution on International trade and development, paragraph 10 (adopted on 2 December 1996).

[23] CSD, Decision 4/1 on Trade, Environment and Sustainable Development, paragraph 4.e. Commission on Sustainable Development, Report on the Fourth Session (18 April - 3 May 1996). E/1996/28 and E/CN.17/1996/38.

measures.

49. The CSD, at its fourth session, inter alia stressed the importance of capacity building and support for national efforts aimed at internalizing environmental costs. The UNCTAD secretariat has been cooperating with UNDP in the preparation of a monograph on capacity-building on trade, environment and sustainable development, in the context of UNDP's Capacity 21 Programme.[24] A description of UNCTAD's own activities in the area of capacity building is provided in report TD/B/COM.1/Misc. 2.[25]

III. OUTSTANDING ISSUES

50. This section examines some cross-cutting issues emerging from the current debate on trade, environment and development, which require further analysis. The intention of this section is to facilitate consideration of the direction of the future debate, taking into account the difficulties of arriving at a consensus on a number of issues. Some, but not all, aspects of these outstanding issues may be analyzed as part of UNCTAD's programme of work.

A. Trade liberalization and market access

51. As part UNCED progress in the provision of additional financial resources and access to and transfer of technology to developing countries has not been encouraging, trade liberalization and improved market access have become even more necessary as a means of generating sources of financing for sustainable development.

52. Trade liberalization initiatives should be accompanied by measures aimed at enhancing the trade performance of low-income, commodity-dependent countries and other countries which remain marginal participants in world trade, in particular the least developed countries. The expansion and diversification of export opportunities, including diversification into higher value-added products, could help these countries in their efforts to both reduce poverty and protect the environment. Trade liberalization measures should be complemented by policies and measures aimed at assisting these countries to improve their supply capacity, promote structural change, increase competitiveness and strengthen the ability of industries to take advantage of market opportunities.

53. The CSD, at its fourth session, invited "UNCTAD, in cooperation with UNEP and other relevant organizations, such as OECD, taking into account the work already under way at the WTO, to examine how further trade liberalization, such as through the reduction or elimination of tariff escalation, export taxes or restrictions, trade-distortive subsidies and the elimination of tariff and non-tariff barriers to trade, can result in environmental benefits and contribute to sustainable development, including by examining recent analyses on these topics".[26] Further empirical work and analysis in these areas could focus on the reduction and removal of remaining trade restrictions and distortions in sectors and products in which developing countries have a particular export interest, such as textiles and clothing, leather and leather products, footwear, forest products, fish and fish products, minerals and mining products, agricultural products, other natural resource-based products and primary commodities.

54. In addition, enhanced market access could be granted for some sectors like

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[24] UNDP is issuing a series of sectoral Capacity 21 monographs, which serve as a tool to advance the thinking and understanding of capacity-building for environment and natural resources management in relation to various social goals and economic sectors.

[25] In the area of technical assistance, UNCTAD IX mandated UNCTAD to assist developing countries in trade and environment, including through country studies (Final document of UNCTAD IX, paragraph 97(ii), second indent).

[26] CSD, op. cit., Para. 7(c).

wood products, fisheries and agriculture, particularly to developing countries having better environmental absorptive capacities, thereby enhancing their income and generating environmental protection at a global level.[27] Potential economic and environmental benefits would accrue from the reduction and removal of tariff escalation by helping to raise the value added by producers in commodity-dependent countries, increase incomes in those countries, and reduce direct pressure on natural resource exploitation.

55. In the context of the MTS, it may be worth examining how developing countries, in particular LDCs, could benefit from provisions concerning differential schedules for compliance with trade-related environmental measures, such as time limited exceptions, or the use of a de minimis clause. In addition, there is a need to examine options for increasing market access for environmentally friendly products from developing countries and promoting the development and transfer of environmentally-sound technologies.

56. Further analysis should focus on specific sectors of export interest to developing countries and SMEs. Future work should also focus on the environmental benefits improving market access, by (a) providing additional market access, including for environment-friendly products, and (b) removing trade restrictions and distortions, an issue which overlaps with that of trade liberalization and the environment.

B. The PPM issue

57. Discussions have focused on the treatment of standards based on non-product-related process and production methods (PPMs) in the trade and environment interface. For example, one of the critical issues in the debate on eco-labelling is the treatment of PPMs. Similarly, in the future debate on competitiveness, border adjustments for PPM-based taxes may become a contentious issue. In addition, with regard to market access, PPMs are an important factor which in many cases distinguish environmental requirements from other technical standards.

58. Since a large part of environmental effects appears to be associated with the production process, rather than with the product, standards on PPMs are of key importance. However, to the extent that environmental effects are intrinsically local, using the same standard across countries or regions, or even within a country, may not be appropriate, in particular because standards can be more effective if they take account of the environmental and developmental conditions to which they apply. Therefore, using trade measures based on PPMs may not meet the environmental objectives which they are designed to meet. Thus, from an environmental point of view, the case for harmonization is not very strong. Where environmental problems are of a global nature, the principle of common but differentiated responsibilities could be taken to mean either that differing standards could be used to achieve a common environmental goal or that developing countries should receive financial assistance to bear incremental costs of implementing the multilaterally-agreed standard.

59. From a trade point of view, there is concern that harmonization of PPMs could undermine comparative advantage, which is the very basis of welfare gains derived from international trade. Applying PPM-based standards to imported products could also involve the extraterritorial application of domestic environmental law. It also raises concerns as to whether the use of non-product related PPMs in the context of the environment would set a precedent for the pursuit of other non-trade related objectives through the use of trade restrictions based on PPMs. For these reasons, making market access conditional on the use of particular PPMs is generally considered incompatible with existing trade rules. Additionally, compliance with specific non-product related PPMs in the context of either eco-labelling or other similar standards could require the use of specific technologies. Therefore some have expressed the view that concerns about the possible discriminatory character of PPM-based standards could be magnified, depending on the degree of patent protection of specific

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[27] See also WTO, op. cit., para. 198.

technologies.

60. It seems reasonable that, from a development perspective, PPM-based standards should be commensurate with a country's environmental problems, environmental absorptive capacity, economic resources and social preferences. In this context, it is also worth noting that certain instruments which are used in developed countries to influence PPMs may be less effective in many developing countries. Policies and measures aimed directly at increasing the capacity of firms to improve their environmental performance, such as building environmental infrastructure for SMEs, may yield greater benefits in economic and in environmental terms.

61. Experience from UNCTAD studies shows that trade and investment links with countries where environmental requirements are relatively stringent may have positive effects on environmental characteristics of PPMs in the exporting country. Thus, trade and investment can play a role in promoting environmentally preferable PPMs worldwide, provided that PPMs are also useful in the context of the environmental and developmental conditions in the country of production. Since it is generally agreed that unilateral trade restrictions should not be used to influence PPMs outside a country's own territory, the debate on PPMs should be based on pragmatic approaches, positive measures, and international cooperative approaches, including in the context of FDI, rather than being situated in the context of trade rules.

62. Future work on PPMs could include a consideration of such issues as the relationship between PPMs and trade, including a consideration of trade principles which could ensure that the application of PPM-based instruments do not result in arbitrary discrimination or unjustified restrictions on trade. A second issue is whether international standards developed for instruments and measures which extend to PPMs, such as the ISO 14000 series, could provide sufficient guarantee to this effect. A third issue that arises is: if there is a consensus to move towards a larger convergence of PPMs, what would be an appropriate mechanism to do so, and what would be the role of FDI, taking into account the interests of all parties with different environmental endowments and at different levels of development.

C. Environment for development

63. The international community should be aware of and respond adequately to the challenge developing countries are facing in making trade and environment mutually supportive by forging sustainable paths of growth and development in a more global and liberalized world economy. In this context, the key role that the promotion of trade and mutual benefit approaches between countries at different stages of economic development can play in making environmental goals a vehicle to sustainable development should be better understood and encouraged.

64. In section II, two categories of positive measures have been defined for analytical purposes. A first category aims at countering adverse income and developmental effects of environmental policies and measures. Such measures are effective in facilitating the introduction of more stringent environmental standards and in rendering environmental policies easier to enforce and more efficient. Both categories also play a key role in ensuring that equity considerations are taken into account; for example, in keeping with the principle of common but differentiated responsibilities, positive measures have been incorporated into MEAs.

65. Realizing the full potential that mutually supportive environmental and trade policies can make to sustainable development, however, requires a broader concept of positive measures, including appropriate economic instruments, incentive measures and mutually beneficial partnership-type approaches, fully involving the private sector and the civil society. Such measures may be relatively easy to implement, since they do not necessarily require lengthy international negotiations. In addition, they may be particularly effective in the long run in that they are self-sustained by promoting endogenous and market-based forces which strengthen positive linkages between environmental measures, trade and sustainable development.

66. With a view to promoting "environment for development", suggested area for further work by UNCTAD could include an overview of the work on trade i biological resources (BIOTRADE) as well as work in the field of resourc management, internalization and the promotion of trading opportunities fo environment-friendly products.

67. Most of the debate on internalization has focused on negativ environmental externalities (ie. costs); the case of positive externalities (i.e benefits) has received less attention. Environmental benefits are often provide to third countries, without the exporting country receiving appropriate payment Positive environmental externalities indicate a market failure because prices o goods and services derived from these resources do not fully reflect socia gains.

68. One of the clearest examples of positive environmental externalities provided by natural ecosystems, since they provide a wide range of local national and international benefits, including watershed protection, ecotourism revenues, and carbon sequestration. However, because of the existence of marke failures, these benefits often do not provide central governments or local populations with sufficient economic incentives to preserve primary forests wetlands, coral reefs and other biological diverse ecosystems.

69. Policy-makers have therefore increasingly focused on positive measure which facilitate the use of market mechanisms and financial incentives to capture the numerous external benefits provided by biologically diverse ecosystems. These mechanisms include debt for nature swaps, transferable development rights green taxes on ecotourist activities, watershed protection payments, and package harvest rights in protected areas. The emergence of an active bioprospecting market can provide an additional means of converting the potential future value of biodiversity into current income for those most responsible for and most affected by the preservation of biologically diverse ecosystems. However, simply creating a market for trade in biological material may not itself generate significant conservation incentives or benefits for the host country; this will require close attention to economic and market research, alternative contractual arrangements and guidelines on access to biological and genetic resources, training and capacity building, the promotion of incentive measures for benefit sharing, access to and transfer of technology related to the development of bioresource industries in developing countries, as well as data dissemination and networking.

70. An important element in this connection is improvement in the capabilities of developing countries to compete in the emerging market for biological resources, while reducing transaction costs and increasing demand for biochemical resources. Under the heading of BIOTRADE, the UNCTAD secretariat is working towards such as improvement through a collaborative effort with the Secretariat of the Convention on Biological Diversity (CBD), interested United Nations agencies and other intergovernmental and non-governmental organizations, the private sector, local communities and academic institutions.[28]

71. The CSD, at its fourth session, expressed support for BIOTRADE, stating that "in regard to biological diversity and trade issues, the Commission welcomes BIOTRADE ... and encourages further consultations on this matter."[29] In response, the UNCTAD secretariat presented BIOTRADE at the III Meeting of the Conference of the Parties to the Convention on Biological Diversity (COP III

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[28] In March 1996, at the OECD International Conference on Economic Incentives for Biodiversity held in Cairns, Australia, general support was expressed for the concept of BIOTRADE.

[29] CSD, op.cit, para. 9.

held in Buenos Aires (4 to 15 November 1996).[10] Positive reactions to BIOTRADE were expressed during the discussions under various agenda items, in particular by the Group of 77 and China, and several developed and developing countries. COP III stressed the need for close coordination with UNCTAD in the fields of access to genetic resources[11] and incentive measures[12].

72. In the field of commodities, in response to the Decision on Trade, Environment and Development adopted by the CSD at its fourth session, the UNCTAD secretariat's has been pursuing sectoral round tables and other informal arrangements for identifying efficient and cost-effective approaches to internalization of environmental cost and benefits and their reflection in international commodity prices. It is suggested that this work be intensified in the future.

D. Positive measures and multilateral agreements

73. This report has made extensive reference to positive measures to achieve the objectives of MEAs as well as to address local environmental problems. An important question is what are the possibilities which multilateral legal instruments, in particular MEAs and the multilateral trading system (MTS), provide for the effective implementation of such measures at the national and international levels. It is important to note that while trade measures normally have a binding character, experience with the implementation of MEAs shows that positive measures are, in general, non-binding: there are no enforcement mechanisms.

74. In the context of MEAs, it is important to design and encourage mechanisms aimed at ensuring that positive measures are fully implemented. It is also important to promote voluntary measures to help in achieving the objectives of the MEA. In this context, the Ad Hoc Working Group on Trade, Environment and Development discussed incentives that encourage trade in environmentally-friendly substitutes, voluntary mechanisms on foreign direct investment and technology transfer, and market-based instruments.

75. The provisions of the multilateral trading system provide ample opportunities for the implementation of positive measures, for example in the area of transparency and additional market access. Furthermore, in accordance with the Agreement on Subsidies and Countervailing Measures (SCM), under certain conditions, subsidies may be provided to assist firms in adapting existing production facilities to new environmental requirements imposed by law and/or regulations. In addition, under certain conditions, subsidies granted to SMEs could be regarded as "non-specific",[13] i.e. "non-actionable".

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[10] At the III Meeting of the Conference of the Parties to the CBD, BIOTRADE was presented in a Workshop organized by UNCTAD on 7 November 1996 (See UNEP/CBD/COP/3/Inf-49), 21 October 1996.

[11] The COP III Decision on Access to Genetic Resources urges the Executive Secretary to coordinate closely with the FAO, UNCTAD, and other relevant organizations working on access to genetic resources to ensure complementary efforts. UNEP/CBD/COP/3/L.7, 13 Nov. 1996, para. 9.

[12] The COP III Decision on Incentive Measures requests the Executive Secretary to take into consideration relevant work under way in other fora such as UNCTAD and OECD. UNEP/CBD/COP/3/L.11, Nov. 1996, para. 9.

[13] The definition of "specificity" of a subsidy is provided in Article 2 of the Subsidies and Countervailing Duties Agreement. Briefly, for a subsidy to be regarded as non-specific, it should (a) be generally available (i.e not limited to certain enterprises or industries); and (b) be granted according to an eligibility criteria that is objective and neutral. Footnote 2 of Article 2 describes objective and neutral criteria as criteria which do not favour certain enterprises over others and which are economic in nature and horizontal in application such as employees or size of enterprise. (Emphasis added.)

76. In this context, it would also be useful to examine how developing countries could benefit from existing provisions on special and differential treatment under various WTO agreements, such as the TBT Agreement (e.g. differential schedules for compliance with trade-related environmental measures, such as time limited exceptions). It might also be useful to examine the relevance for sustainable development of the provisions of "Part IV" of the GATT, which contains special provisions on actions that could be taken by developed countries to promote the trade and development of developing countries.[14]

77. Future work would need to identify: (a) provisions in the international trading system which could be used to promote the use of positive measures; (b) how to design, and ensure full implementation of, positive measures in MEAs.

E. Trade, investment, and environment

78. Apart from providing additional resources that can contribute to sustainable development, foreign direct investment (FDI) has an important role to play in providing host countries, particularly developing countries, with easier access to environmentally sound technologies and management practices. There is ample scope for developing positive synergies between trade, environment, and investment policies to promote sustainable development.

79. The early debate on the relationship between foreign direct investment (FDI) and the environment largely focused on the issue of "dirty industry migration". More recently, discussions have focused on the issue of technologies and management practices associated with FDI. According to one hypothesis, transnational corporations (TNCs) tend to apply the environmental standards and management practices of the corporation or the home country, which often go beyond local legal requirements in the host country. According to another hypothesis, however, trade liberalization and FDI can at times result in the transfer of technologies and products (to developing countries) which have become "obsolete" as a result of increasingly stringent environmental policies and regulations in developed countries.

80. From an environmental point of view, a distinction needs to be made between local and global environmental problems. From the point of view of local environmental problems, FDI can have either positive or negative effects. Policies for fostering their positive effects should be encouraged. Where they have potentially negative effects, appropriate policies on the part of the host country as well as responsible environmental behaviour of investors, should be encouraged, for example through voluntary mechanisms. As far as global problems are concerned, there is a considerable potential for generating win-win scenarios if foreign investors also transfer best environmental practices and technologies in order to enable developing countries to meet their commitments under MEAs. For example, according to a recent UNEP report, many Japanese, North American and European automobile, chemical, consumer product, electronics, and petroleum companies pledged to help the Government of Viet Nam to protect the ozone layer by investing only in modern, environmentally friendly technology in their Viet

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[14] Article XXXVI, "Principles and Objectives", recognizes the need to provide developing countries with improved market access for primary products (including agricultural products) and for processed and manufactured products of export interest to them. It also recognizes the need to take measures, whenever appropriate, to "attain stable, equitable and remunerative prices" for primary products. Article XXXVII, "Commitments" provides that developed countries should, to the fullest extent possible, accord high priority to the reduction and elimination of tariffs and non-tariff barriers on products of potential export interest to developing countries, as well as to give active consideration to the adoption of other measures to provide greater scope for imports from developing countries. Article XXXVIII, lists forms of "Joint Action" that WTO members can undertake, for example in the area of commodities (for improved market access and stabilization of prices at equitable and fair levels).

Nam projects.[15] More work is also needed to develop cost effective mechanisms which could be environmentally beneficial. Discussions on such mechanisms, e.g pilot projects on joint implementation, are under way in the context of the Framework Convention on Climate Change.

81. From a trade point of view, it is generally held that trade liberalization and economic openness encourage a more efficient allocation of resources worldwide, by allowing goods, services and investment to move more freely across borders and to respond to market-driven incentives. As trade liberalization is generally accompanied by more open policies and increased foreign direct investment, it is important to ensure that such investment increases the capacity of host countries to respond to domestic environmental needs as well as to external environmental requirements, including in the framework of MEAs.

82. From a development point of view, FDI can be an important instrument to disseminate efficient and state-of-the-art environmentally sound production processes and methods to developing countries. On the other hand, there is concern about the movement of obsolete equipment and technologies to them, even though there may be little evidence on dirty industry migration to developing countries. Some concerns about "technology dumping" have also arisen in the context of multilateral environmental agreements.[16] In cases where FDI is associated with technologies which are not up-to-date from an environmental point of view, possible economic gains from increased FDI have to be weighed against possible costs. Transparency is needed to allow developing countries to take informed decisions.

83. It is important to identify policies and measures aimed at maximizing the contribution that FDI can make to promoting access to and the transfer of ESTs to developing countries. Further work could focus on (a) empirical studies on the environmental practices associated with FDI; (b) designing policies and measures to promote the transfer of environmentally sound technologies and environmentally sound practices through FDI; and (c) identifying positive synergies between policies which promote trade liberalization, investment, and environmental policies.

F. Small and medium-sized enterprises (SMEs)

84. Discussions and analysis so far have recognized the special situation of SMEs in the trade and environment interface. The high rate of participation of SMEs in exports from many developing countries as well as the special circumstances of their operation make it imperative that the design of environmental policies take account of their special conditions. Measures for SMEs could be divided into three categories: (a) short-run (b) medium-term and (c) long-run. In the short run there may be a need to grant more leeway to SMEs when more stringent standards are applied to the sector or the country or as a whole. In the medium term, capacity-building, technical assistance and special financing programmes could focus on SMEs. In the long run, SMEs in developing countries need to address issues such as lack of financial assistance, lack of technology and the low quality of their products.

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[15] UNEP, Technology and Economic Assessment Panel. Report to the Parties. November 1995, page II-23.

[16] According to a memorandum submitted by Duncan Brack to the Environment Committee of the House of Commons session 1995-1996, Fourth Report on World Trade and Environment, Vol. 2, Minutes of Evidence and Appendices, p. 264, "Although, .. there is no real evidence for the migration of industries to developing countries to escape the controls on ODS, there is substantial evidence to suggest that equipment rendered obsolete by the controls is being moved. ... although such movement of obsolete technology itself is not illegal, it helps to undermine countries' efforts to implement accelerated phaseout schedules. Furthermore, anecdotal evidence suggests that some second hand equipment, such as domestic refrigerators, is being illicitly shipped to developing countries by firms paid to break them up and dispose of the refrigerants."

85. If SMEs are spatially dispersed it may not be necessary to treat them with the same sense of urgency as large firms in the course of implementing higher domestic environmental standards. It may also be useful to examine whether and how the principle of common but differentiated responsibility would apply to SMEs both in a local and in a global context.

86. From a trade point of view, in general no distinction is made between SMEs and large firms in the body of trade rules. As mentioned in section D above, some special provisions exist in the Agreement on Subsidies and Countervailing Measures (SCMs) which could also be used for SMEs. However, given that the resources for granting subsidies are relatively limited in developing countries, it may be necessary to examine whether other allowances on the lines of part IV of the WTO Agreement can be extended to SMEs. Technological assistance from small scale units in developed countries to those in developing countries could also be of benefit. Another alternative being explored in order to facilitate the adaptation to environmental standards is to encourage the transfer of FDI to SMEs in developing countries.

87. From a development perspective, there may be a trade-off between promoting SMEs for employment and poverty alleviation objectives and investing in expensive chemicals and cleaning processes in response to export requirements.[17] Finding cost-effective chemicals (e.g. natural chemicals) and reducing the effluent at source in the small-scale sector in the textiles and leather sectors, for example need to be explored. In this sector it is specially important to identify win-win opportunities, as SMEs are important engines of economic growth. Incentives can also be granted to encourage SMEs to invest in environmental improvements.

88. Issues deserving future analysis are (a) whether there is a need to accord special treatment to SMEs in both MEAs and in the multilateral trading system in the course of raising environmental standards; (b) whether special trading opportunities would assist SMEs in moving to higher environmental standards; and (c) what should be the basic features in the design of a package of measures for SMEs in order to ensure that they integrate the objectives of trade, environment, and development.

IV. CONCLUSIONS AND RECOMMENDATIONS

89. This report reviews progress in integrating trade, environment and development since UNCED. Section II has examines developments in the field of competitiveness, market access, eco-labelling, multilateral environmental agreements, positive measures and the relationship between trade liberalization and sustainable development. It indicates that, while more analysis is needed, progress has been made in better understanding these issues.

90. Section II suggests that, with regard to the evolution of the trade and environment debate, two observations are relevant. First, some of the issues which earlier were viewed by some as a potential source of conflict are no longer so. Examples can be found in particular in the competitiveness debate (e.g. on issues such as "eco-dumping" or "green" countervailing duties). Secondly, in the analysis of different issues, a number of common concerns have emerged, such as the special situation of SMEs in the trade and environment interface, the need to identify "win-win" situations and the important role of positive measures. Thus, focusing analysis on these topics may be an appropriate way to help advance an understanding of outstanding issues.

91. Section III identifies some cross-cutting issues which could be the subject of further examination, including in UNCTAD. It examines pragmatic approaches to integrating trade, environment and development, for example with regard to the issue of PPMs, the special situation of SMEs in the trade and environment interface, and competitiveness concerns related to future environmental policies and measures. In particular it examines the role of investment, incentives, economic instruments, and other initiatives in broadening

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[17] Manas Bhattacharyya, op.cit

the options for the effective implementation of a wide range of positive measures. For example, UNCTAD's work on trade in biological resources, the examination of successful experiences with the internalization of environmental costs and benefits in the area of commodities, as well as multi-sectoral and sector-specific round tables can help to identify appropriate enabling measures for harnessing the synergies between trade liberalization, economic reform and sustainable management of natural resources are especially relevant.

A. Conclusions

92. Analysis and debate have contributed to a better understanding of trade and environment linkages. While further analysis and deliberations are required, the following conclusions could be offered at this stage:

(a) Important progress has been made in understanding the relationship between trade, environment and development. Throughout the debate, Governments and the civil society have reiterated their commitments to both trade liberalization and environmental protection. The principles contained in the Rio Declaration and Agenda 21, as well as the principles of the multilateral trading system have been strongly endorsed; the international community has continued to strongly reject unilaterism and to seek multilateral cooperative approaches. Despite differing priorities across countries, it has been possible to achieve a balance in the trade and environment debate while keeping the momentum generated in the post-UNCED process.

(b) There has been growing consensus in intergovernmental deliberations that positive measures are effective instruments to assist developing countries in their efforts to achieve the objectives of sustainable development.

(c) The competitiveness debate has evolved in its emphasis. Some issues have been set aside. The need to comply with environmental requirements emerging from developed country markets continues to raise competitiveness and market access concerns for developing countries.

(d) Small and medium-sized enterprises (SMEs) often make a relatively large contribution to industrial pollution. SMEs may encounter special difficulties in responding to environmental challenges. At the same time, there is considerable potential for improving environmental management in SMEs provided that proper supporting infrastructure, including access to finance, technology and information is set up.

(e) There is no empirical evidence to suggest that existing environmental policies have widespread effects on market access. However, effects could be more significant for some sectors and for small and medium-sized enterprises. Additional market access, particularly for products from developing countries, could generate environmental benefits.

(f) Progress has been made on market access, in particular by completing the Uruguay Round negotiations. Timely and full implementation has an important role to play in promoting sustainable development through trade. As progress in other areas identified in Agenda 21, such as the provision of additional financial resources and access to and transfer of technology, has faced a number of constraints, trade liberalization and improved market access have become even more necessary as a means of generating sources of financing for sustainable development.

(g) The effects of trade liberalization on the environment are unlikely to be either universally positive or negative; they will probably differ by country, sector and commodity in question. Additional environmental benefits would accrue to developing countries from trade liberalization, on account of income and technology effects. Trade liberalization could also be a catalyst in implementing domestic policy reforms in both developed and developing countries, resulting in further environmental benefits.

(h) The debate on eco-labelling has highlighted the sensitivity surrounding the issue of standards concerning non-product-related process and production methods (PPMs). Progress has been made in building consensus on the need to move to a broader concept of transparency. In addition, the ISO has made progress in developing multilaterally agreed guidelines. However, little or no progress has been made on building consensus on how to deal with the issue of non-product-related PPMs and on the concept of equivalency. This raises the question how future discussions on non-product-related PPMs should be handled.

(i) A wide range of policy instruments, including positive measures, can be used (often as a package of measures) to achieve the environmental objectives of multilateral environmental agreements (MEAs). It is difficult to assess the environmental effectiveness and economic efficiency of individual policy instruments used in MEAs. This should not, however, prevent attempts to take stock of the effectiveness of the instruments and their economic and social costs, with a view to identifying measures to reducing these costs.

(j) Internalizing positive externalities may result both in enhanced environmental protection and in generating additional resources for developing countries. UNCTAD's work on trade in biological resources (BIOTRADE), which is a collaborative effort with the CBD secretariat, aims at promoting both the conservation of biological resources and increasing the capacity of developing countries to compete in the emerging market for biological resources.

(k) There is a need to identify efficient and cost-effective approaches to internalization of environmental cost and benefits, in particular in the commodities sector. Round tables and other informal arrangements for their reflection in international commodity prices, as well as promoting trade in environmentally preferable products, are also relevant in this context.

B. Recommendations

93. In the light of the above conclusions, the following recommendations are put forward for consideration by the Commission:

(a) There should be a balanced and integrated approach to environment, trade and development issues[18]. The debate may have to move from the stage of problem identification to problem solution. In this context, the sustainable development agenda should focus on the promotion rather than on the restriction of trade and investment, building on synergies between trade liberalization, economic reform, and improved management of natural resources and the environment. There is a need to promote the involvement of the business community and the civil society in the design of specific enabling measures, including through technical assistance activities.

(b) In order to promote the integration of trade, environment and development policies, certain principles should be applied in the design and implementation of environmental policies with trade effects. There is a need to explore further a number of principles and concepts, such as transparency, least trade restrictiveness, proportionality, equivalency and mutual recognition. There is also a need to examine the relationship between environmental and trade principles.

(c) Further work on competitiveness and market access, including by UNCTAD, should inter alia take into account the special needs and concerns of developing countries, particularly as regards SMEs as well as particular sectors. Future work could also include an identification and analysis

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[18] General Assembly, Resolution on International Trade and Development, paragraph 9. (adopted on 2 December 1996)

of win-win situations.

(d) Efforts to integrate trade and environment should pay particular attention to the special conditions and needs of SMEs. Similarly, it is important to ensure that SMEs have adequate access to any enabling measures, including in the framework of MEAs.

(e) Further trade liberalization could be implemented by improving market access conditions, including for environment-friendly products; and by removing trade restrictions and distortions with a view to facilitating the achievement of environmental benefits and contributing to sustainable development. In examining how trade liberalization can result in environmental benefits and contribute to sustainable development, UNCTAD should focus on specific sectors of export interest to developing countries.

(f) Trade liberalization initiatives should pay special attention to enhancing the trade performance of low-income, commodity-dependent countries and other countries which remain marginal participants in world trade, in particular the least developed countries. The expansion and diversification of export opportunities, including diversification into higher value-added products, could help these countries in their efforts both to reduce poverty and to protect the environment.

(g) More empirical analyses on the economic effects of MEAs are needed, including through studies undertaken by UNCTAD, in cooperation with UNEP. Such studies should also assess the effects of trade and other policy instruments in MEAs on the achievement of environmental goals and on economic development.

(h) In accordance with its mandate, UNCTAD should propose positive measures at the national and international levels to promote the efforts of developing countries to achieve the objectives of sustainable development. A wide range of such measures can be explored, including enabling measures at the national level, the promotion of trade in environmentally preferable products, pragmatic and cost-effective approaches to internalization of costs and benefits, in particular in the commodity sector. Promising avenues for the promotion of positive measures are also being developed in UNCTAD's work on trade in biological resources (BIOTRADE);

(i) Positive measures, which have been incorporated into several MEAs, are not generally of a binding character; initiatives may be necessary to promote the effective implementation of positive measures. For example, MEAs could provide incentives and specific mechanisms for facilitating technology transfer. There may also be a need for increased involvement of developing countries in the design and implementation of positive measures.

(j) Since it is generally agreed that unilateral trade restrictions should not be used to influence PPMs outside a country's own territory, the debate on PPMs should be based on pragmatic approaches, positive measures, and international cooperative approaches, including in the context of FDI, rather than being situated in the context of trade rules.

(k) It would be useful to undertake an analysis of the role of foreign direct investment (FDI) in promoting access to and transfer of environmentally sound technologies, thereby assisting developing countries in responding effectively to environmental challenges, including in the context of MEAs. Therefore, in the context of work on positive measures, more analysis is needed to identify policies and measures aimed at maximizing the role that FDI can play in supporting developing countries in their efforts to achieve the objectives of sustainable development.